

Message Text

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PAGE 01 TAIPEI 00834 110253Z

61

ACTION EA-14

INFO OCT-01 ISO-00 FEA-02 INT-08 SPC-03 SAM-01 AID-20

EB-11 NSC-10 RSC-01 CIEP-02 TRSE-00 SS-20 STR-08

OMB-01 CEA-02 CIAE-00 COME-00 FRB-02 INR-10 NSAE-00

XMB-07 OPIC-12 LAB-06 SIL-01 DODE-00 PA-04 USIA-15

PRS-01 AGR-20 DRC-01 /183 W
----- 119261

R 090650Z FEB 74

FM AMEMBASSY TAIPEI

TO SECSTATE WASHDC 904

INFO AMCONSUL HONG KONG

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E.O. 11652: NA

TAGS: ECON, TW

SUBJECT: INITIAL EFFECTS OF ECONOMIC STABILIZATION MEASURES OF
JANUARY 26

REF: TAIPEI 607

HONG KONG FOR TREASURY REP

1. BEGIN SUMMARY. GRC'S COMPREHENSIVE STABILITZTION PROGRAM
HAS PROMPTED CAUTION THROUGHOUT TAIWAN WHILE PEOPLE TRY TO
SORT OUT IMPACT. AS ANTICIPATED BOTH WAGES AND PRICES HAVE
INCREASED, IN SOME CASES DRASTICALLY. THERE HAVE BEEN
ISOLATED REPORTS OF HOARDING, PROFITEERING AND PANIC BUYING
PARTICULARLY OF FOODSTUFFS. MANUFACTURING SECTOR IS ADOPTING
A "WAIT AND SEE" ATTITUDE ABOUT FUTURE INVESTMENT. PURCHASES
OF NON-ESSENTIAL CONSUMER GOODS HAVE DECLINED PERCEPTIBLY
OWING TO PUBLIC RESISTANCE TO HIGHER PRICES. PRELIMINARY
INDICATIONS ARE THAT FINANCIAL MEASURES ARE BEGINNING TO HAVE
DESIRED EFFECT; SAVINGS DEPOSITS INCREASED 1 PERCENT IN ONE
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PAGE 02 TAIPEI 00834 110253Z

WEEK, DOUBLE THE USUAL RATE. ONLY MAJOR ERROR SO FAR IN

GOVERNMENT HANDLING WAS THE BELATEDNESS OF ITS INTERVENTION OF OFFSET SPECTACULAR INCREASE IN PSYCHOLOGICALLY IMPORTANT RICE PRICES.

2. EMBASSY REMAINS RELATIVELY SANGUINE ABOUT

ECONOMIC STABILIZATION MEASURES. INITIAL SURGE IN PRICES--THOUGH EXPECTED BY GOVERNMENT--HAS UNDERCUT PUBLIC CONFIDENCE THAT GOVERNMENT'S ONE SHOT PROGRAM WILL HALT INFLATION. HOWEVER, EVEN MOST SEVERE CRITICS ARE RESERVING JUDGMENT. PERHAPS MOST HELPFUL NEWS FOR GOVERNMENT SO FAR IS STRONG CONSUMER RESISTANCE TO RISING PRICES AND EVIDENCE THAT THERE HAS BEEN SUBSTANTIAL INCREASE IN RATE OF SAVINGS. END SUMMARY.

3. FIRST TWO WEEKS OF GOVERNMENT'S EXPERIMENT WITH COMPREHENSIVE STABILIZATION PROGRAM HAVE BEEN MARKED BY CAUTION IN ALL QUARTERS AS PEOPLE TRY TO SORT OUT THE IMPACT.

GOVERNMENT LEWFTS

HAVE MAINTAINED CONFIDENT AND RATHER BENEVOLENT POSTURE IN FACE OF SOME UNEXPECTED DIFFICULTIES, SUCH AS SKYROCKETING RICE PRICES. DESPITE CONSIDERABLE DOUBT THAT ONE SHOT PROGRAM WILL HALT INFLATION, THERE IS NO SENSE OF PANIC AND EVEN MOST SEVERE CRITICS ARE RESERVING JUDGMENT ABOUT WISDOM OF NEW MEASURES. FOLLOWING IS SUMMARY OF DEVELOPMENTS IN KEY AREAS:

A. WAGES-10 PERCENT WAGE INCREASE AND SPECIAL BONUS FOR CIVILIAN AND MILITARY GOVERNMENT PERSONNEL HAS IMPELLED MANY PRIVATE EMPLOYERS TO GRANT WAGE INCREASES. SEVERAL US AND LOCAL COMPANIES CONTACTED BY EMBASSY AND IT APPEARS AVERAGE INCREASE HAS BEEN APPROXIMATELY 20 PERCENT PLUS ADDITIONAL AMOUNT FOR FOOD SUPPLEMENT. SINCE STRIKES ARE ILLEGAL AND BARGAINING POWER OF EMPLOYEES IS WEAK, THERE HAVE BEEN NO INSTANCES OF OPEN LABOR UNREST. HOWEVER,, MANAGERS OF SEVERAL MAJOR COMPANIES REPORT THAT INITIAL OFFER OF 10 PERCENT WAGE INCREASE RESULTED IN MASSIVE SLOWDOWN AND DECLINE IN PRODUCTIVITY.

B. CONTROLLED PRICES-FURTHER ADJUSTMENTS UPWARD PROBABLY WILL BE REQUIRED FOR SEVERAL ITEMS UNDER PRICE CONTROL, NOTABLY PORK AND FERTILIZERS. BECAUSE OF HIGHER COSTS, FARMERS REPORTEDLY ARE HOLDING HOGS OFF MARKET AND LIMITED OFFICIAL USE

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PAGE 03 TAIPEI 00834 110253Z

DISTRIBUTORS ARE HOLDING BACK UREA AND AMMONIA SULPHATE FERTILIZERS UNTIL NEW NEGOTIATED PRICES ARE ESTABLISHED TO REPLACE CEILING PRICES IMPOSED JULY 1. IN MEANTIME, BLACK MARKET HAS DEVELOPED FOR BOTH PRODUCTS WITH PORK PRICES RISING 70-100 PERCENT OVER PRE-JANUARY 26 LEVEL.

C. UNCONTROLLED PRICES-PRICES OF ITMES NOT ON CONTROLLED LIST, HAVE SKYROCKETED SINCE JANUARY 26.

MAGNITUDE OF INCREASES IN MOST CASES IS NOT JUSTIFIABLE ON ECONOMIC GROUNDS. FRUIT AND VEGETABLE PRICES HAVE REMAINED RELATIVELY STABLE. RICE, HOWEVER, INCREASED ALMOST 400 PERCENT BETWEEN JANUARY 28 AND FEBRUARY 4 IN TAIPEI AREA. SINCE RICE IS MOST IMPORTANT SINGLE ITEM IN LOCAL DIET, GRC BELATEDLY RELEASED ADDITIONAL SUPPLIES TO MARKET, AND THREATENED SEVERE PENALTIES TO SPECULATORS AND HOLDERS.

AS OF FEBRUARY 8 PRICE HAD BEGUN TO DECLINE SLOWLY BUT IT IS STILL WAY ABOVE PRE-JANUARY 26 LEVEL. SPOT CHECKS IN SEVERAL LEADING DEPARTMENT STORES AND NUMEROUS SMALL FAMILY-OPERATED BUSINESSES REVEAL THAT PRICES ON CLOTHING, APPLIANCES, JEWELRY AND SUNDRIES, FOR EXAMPLE, HAVE BEEN MARKED-UP BETWEEN 30-40 PERCENT TO LEVEL WHICH MAY HOLD BECAUSE OF CONSUMER RESISTANCE. PRICES IN BARBER SHOPS, BEAUTY PARLORS, GARGES, DRY CLEANERS, RESTAURANTS AND HOTELS HAVE RISEN AN AVERAGE OF 20-30 PERCENT IN TWO WEEKS.

D. MANUFACTURES- WE HAVE NO REPORTS OF PLANT CLOSURES OR REDUCED OPERATIONS AMONG MAJOR US AND LOCAL FIRMS. ALL OF THE 25-30 FIRMS CONTACTED BY THE EMBASSY REPORT THEY EXPECT REDUCED PROFITS IN 1974 BECAUSE OF WAGE INCREASES (MOST HAVE GRANTED INCREASES OF 10-25 PERCENT) AND HIGHER COSTS OF UTILITIES, TRANSPORTATION AND RAW MATERIALS. FIRMS PRODUCING SOLELY FOR EXPORT MARKET ESTIMATE 10-15 PERCENT PRICE INCREASE WOULD NOT HARM COMPETITIVE POSITION ROC EXPORTS SINCE EXPORTS FROM MAJOR COMPETITORS IN ASIA/PACIFIC AREA ALSO ARE BECOMING MORE COSTLY. MAJOR CONCERN OF FIRMS IS THAT MEASURES ANNOUNCED ON JANUARY 26 WILL NOT BE SUFFICIENT TO DAMPEN INFLATION, WITH THE RESULT THAT ADDITIONAL MEASURES WILL HAVE TO BE INTRODUCED IN 1974. PRESIDENT OF ONE MAJOR LOCAL FIRM, WHICH EMPLOYS 2,000 PERSONS IN PACKING AND CANNING AGRICULTURAL PRODUCTS FOR US MARKETS, TOLD EMBASSY THAT HE MAY BE FORCED TO SUSPEND OPERATIONS IF COSTS OF UTILITIES ARE FURTHER INCREASED IN 1974. WE HAVE ALSO RECEIVED SEVERAL REPORTS THAT PRICE UNCERTAINTIES HAVE MADE SOME SUPPLIERS UNABLE TO QUOTE PRICES AGAINST L/C'S.

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PAGE 04 TAIPEI 00834 110253Z

E. EMPLOYMENT-US FIRMS REPORT THAT LABOR TURNOVER RATE IS AT ALL-TIME LOW. WORKERS PRESUMABLY BECOMING MORE INTERESTED IN JOB SECURITY AND SOCIAL BENEFITS OF LONG-TERM EMPLOYMENT THAN IN JUMPING AROUND IN LABOR MARKET.

F. MONEY SUPPLY AND SAVINGS- CENTRAL BANK REPORTED TO EMBASSY INITIAL SUCCESS OF INTEREST RATE POLICY. MONEY SUPPLY ACTUALLY DECREASED 2.3 PERCENT IN 1ST WEEK AFTER JANUARY 27, A REVERSAL OF LONG LASTING TREND. IN SAME WEEK, SAVINGS AND TIME DEPOSITS INCREASED 3 TIMES

USUAL WEEKLY RATE. SAVINGS ALONE INCREASED ABOUT DOUBLE THE RATES FOR ALL OF 1973. ACTUALLY IN LAST QUARTER OF 1973, SAVINGS RATE HAD BEEN NEGATIVE. NO DOUBT IMPROVEMENT PARTLY DUE TO RETRENCHMENT AFTER HIGH LEVEL SPENDING OF BEFORE LUNAR NEW YEAR, BUT SIZE OF CHANGE INDICATES FINANCIAL MEASURES ALSO CONTRIBUTED.

G. INVESTMENT CLIMATE-- MOST MAJOR US AND LOCAL FIRMS HAVE ADOPTED A " WAIT AND SEE" ATTITUDE BEFORE GOING AHEAD WITH NEW INVESTMENT. ONE MAJOR US ELECTRONICS COMPANY ASSERTS IT HAS DECIDED TO EXPAND ELSEWHERE BECAUSE OF UNCERTAINTIES IN THE ROC ECONOMY. SEVERAL OTHERS INDICATE THEY MAY DISINVEST IF GRC IS UNABLE TO HOLD LINE ON WAGES AND PRICES.

4. COMMENT: ALTHOUGH SOME CRITICS AND SOME DEFENDERS HAVE ALREADY JUMPED TO CONCLUSIONS, NO SENSIBLE ASSESSMENT IS POSSIBLE AFTER ONLY TWO WEEKS OF THE GRC'S NEW PROGRAM SHOCK WAVES CAUSED BY THE JAN 26 ANNOUNCEMENT ARE STILL REVERBERATING. NO ONE IN GRC EXPECTED THAT STABILIZATION MEASURES WOULD GO DOWN SMOOTHLY WITH THE PUBLIC OR THAT THERE WOULD BE NO ECONOMIC DISLOCATIONS.

5. GOVERNMENT HAS MADE AT LEAST ONE OBVIOUS MISTAKE. GIVEN THE POLITICAL IMPORTANCE OF RICE, GOVERNMENT SHOULD HAVE INTERVENED IMMEDIATELY IN RICE SITUATION. LIMITED OFFICIAL USE

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PAGE 05 TAIPEI 00834 110253Z

INSTEAD, IT WAITED SEVERAL DAYS HOPING FOR THE RICE MARKET TO RETURN TO NORMAL. PANIC BUYING ENSUED AND THE DANGER OF PUBLIC DISTURBANCES BECAME ACUTE. NOW THE PRICE OF RICE HAS GRADUALLY BEGUN TO DECLINE ALTHOUGH IT IS STILL WELL ABOVE THE PRE-JAN 26 LEVEL.

6. HANDLING OF RICE PROBLEMS HAS BEEN RESPONSIBLE FOR SOME EROSION OF CONFIDENCE IN GOVERNMENT'S ABILITY TO CONTROL INFLATION. THIS SENTIMENT IS PARTICULARLY COMMON IN BUSINESS COMMUNITY. GOVERNMENT PRESUMABLY HAS LEARNED THE LESSON THAT WHILE IT MAY BE PREFERABLE TO LET THE ECONOMY STABILIZE ITSELF WITHOUT GOVERNMENT ACTION, WHEN ACTION IS REQUIRED, IT SHOULD BE PROMPT AND DECISIVE.

7. ALL IN ALL, WE REMAIN RELATIVELY SANGUINE ABOUT EFFECTS OF ECONOMIC STABILIZATION MEASURES. THE INITIAL SURGE IN PRICES HAS ADMINISTERED A CONSIDERABLE SHOCK TO MANY, INCLUDING (ESPECIALLY DOWN-ISLAND) MID-LEVEL GOVERNMENT OFFICIALS WHO ARE THE FIRST TO BE EXPOSED TO POPULAR CRITICISM OF THE GOVERNMENT'S ECONOMIC PERFORMANCE. BUT MANY OF THE INITIAL ADVERSE EFFECTS OF

THE PROGRAM HAVE BEGUN TO MODERATE. STRONG CONSUMER RESISTANCE
TO EXCESSIVELY HIGH PRICES IS BECOMING INCREASINGLY
NOTICEABLE AND IT IS ANTICIPATED THAT SAVINGS WILL RISE
PERCEPTIBLY.
MC CONAUGHY

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Message Attributes

Automatic Decaptioning: X
Capture Date: 01 JAN 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: ECONOMIC DEVELOPMENT, ECONOMIC STABILITY, ECONOMIC PROGRAMS, PROGRAMS (PROJECTS)
Control Number: n/a
Copy: SINGLE
Draft Date: 09 FEB 1974
Decaption Date: 01 JAN 1960
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Authority: morefirh
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 28 MAY 2004
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1974TAIPEI00834
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: N/A
Errors: N/A
Film Number: n/a
From: TAIPEI
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1974/newtext/t19740243/aaaabomy.tel
Line Count: 228
Locator: TEXT ON-LINE
Office: ACTION EA
Original Classification: LIMITED OFFICIAL USE
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 5
Previous Channel Indicators:
Previous Classification: LIMITED OFFICIAL USE
Previous Handling Restrictions: n/a
Reference: TAIPEI 607
Review Action: RELEASED, APPROVED
Review Authority: morefirh
Review Comment: n/a
Review Content Flags:
Review Date: 22 JUL 2002
Review Event:
Review Exemptions: n/a
Review History: RELEASED <22 JUL 2002 by kelleyw0>; APPROVED <22 JUL 2002 by morefirh>
Review Markings:

Declassified/Released
US Department of State
EO Systematic Review
30 JUN 2005

Review Media Identifier:
Review Referrals: n/a
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
Secure: OPEN
Status: NATIVE
Subject: INITIAL EFFECTS OF ECONOMIC STABILIZATION MEASURES OF JANUARY 26
TAGS: ECON, TW
To: STATE
Type: TE
Markings: Declassified/Released US Department of State EO Systematic Review 30 JUN 2005